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SUBJECT: PREVIEW OF EDRC ANNUAL REVIEW OF CANADA, JUNE 4

REF:OECD PARIS 13811

1.ON JUNE 23 MINFIN TURNER WILL PRESENT TO PARLIAMENT NEW BUDGET ORIGINALLY SCHEDULED FOR LATE MAY. BUDGET,WHICH WILL SET TONE AND THRUST OF GOC FISCAL POLICY OVER NEXT SIX TO NINE MONTHS, IS CLOSELY GUARDED SECRET.THUS, CANDEL WILL PROBABLY BE LESS FRANK AND INFORMATIVE THAN USUAL RE GOC ECONOMIC POLICY FOR LAST HALF OF 1975.

2. FEW HINTS THAT TURNER AND PM TRUDEAU HAVE GIVEN RE GOC POLICY TO BE REFLECTED IN BUDGET INDICATE THEIR MOST SERIOUS CONCERN IS INFLATION, PARTICULARLY COST-PUSH ASPECT BROUGHT ABOUT BY HIGH WAGE SETTLEMENTS, AND THEREFORE BUDGET MAY BE SOMEWHAT RESTRICTIVE (E.G., HIGHER TAXES AND/OR LESS GOVERNMENT SPENDING). FOR PAST FEW MONTHS TURNER,AND TO LESSER EXTENT TRUDEAU, HAVE BEEN COMPARING HIGHER WAGE SETTLEMENTS REACHED IN RECENT COLLECTIVE AGREEMENTS IN CANADA WITH LOWER RATE OF INCREASE IN U.S.,AND THEY ARE PRE-
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DICTING THAT CANADIAN GOODS WILL BE NON-COMPETITIVE IN

FUTURE WORLD MARKETS.

3. ESCHEWING WAGE AND PRICE CONTROLS, WHICH WAS MAIN PLATFORM OF OPPOSITION DURING LAST JULY'S ELECTION, GOC LEADERS HAVE TRIED SELL PROGRAM OF VOLUNTARY RESTRAINT. CONSULTATIONS BY TURNER AND OTHER MINISTERS WITH VARIOUS SEGMENTS OF CANADIAN SOCIETY HAVE PRODUCED NO CONSENSUS, AND GENERAL FEELING HERE IS THAT VOLUNTARY PROGRAM HAS BEEN LARGELY REJECTED BY BUSINESS AND LABOR.

4. MOST FINANCIAL ANALYSTS HERE WOULD AGREE WITH OECD SECRETARIAT THAT "1975 WILL BE A DIFFICULT YEAR" FOR CANADA, BUT WOULD DISAGREE WITH PREDICTION THAT REAL GNP WILL FALL 1.4 PERCENT FOR YEAR. MOST PESSIMISTIC FORECAST WE'VE SEEN IS ZERO GROWTH, AND SOME ANALYSTS ARE STILL PREDICTING ONE TO THREE PERCENT GROWTH. ALMOST ALL ANALYSTS AGREE REAL GROWTH WILL RECOMMENCE IN LAST SIX MONTHS OF 1975.

5. RECENT ECONOMIC INDICATORS FOR CANADA ARE SOMEWHAT MIXED BUT DO NOT PRESENT AS GLOOMY SITUATION AS SECRETARIAT CONCLUDES. FOR FIRST QUARTER, REAL DOMESTIC PRODUCT INDEX DROPPED BY 0.0 PERCENT AND MANUFACTURING INDEX WAS OFF BY 2.9 PERCENT. HOWEVER, UNEMPLOYMENT HAS STABILIZED SOMEWHAT AT 7.0 PERCENT FIGURE FOR BOTH MARCH AND APRIL AND CONSUMER PRICE INDEX HAS BEEN RISING MUCH MORE SLOWLY SINCE JANUARY. (SEASONALLY ADJUSTED CPI ROSE 0.5 PERCENT IN JANUARY, 0.7 PERCENT IN FEBRUARY, 0.5 PERCENT IN MARCH AND 0.6 PERCENT IN APRIL). AVERAGE ANNUAL BASE RATE INCREASES IN WAGES DROPPED SLIGHTLY IN THE FIRST QUARTER (16.1 PERCENT VICE 17.4 PERCENT IN FOURTH QUARTER OF 1974).

6. EMBASSY WOULD AGREE WITH MISSION THAT IT SHOULD QUESTION SECRETARIAT'S ASSUMPTION THAT "STIMULATION OF DOMESTIC ECONOMY IS FIRST PRIORITY FOR CANADIAN ECONOMIC POLICY AT PRESENT JUNCTURE." TURNER'S BUDGET OF LAST NOVEMBER WAS STIMULATIVE, INCLUDING INCOME TAX REBATES, TARIFF AND EXCISE TAX REDUCTIONS LIMITED OFFICIAL USE

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AND HOUSING INCENTIVES, AND THESE STIMULI HAVE NOT YET BEEN TOTALLY OBSERVABLE IN ECONOMY. AS TURNER AND OTHER GOC LEADERS HAVE OFTEN STRESSED, STATE OF CANADIAN ECONOMY DEPENDS TO LARGE DEGREE ON ECONOMIC HEALTH OF CHIEF TRADING PARTNERS, NOTABLY U.S., AND RENEWED GROWTH IN THESE COUNTRIES WILL PROVIDE ADDED STIMULUS TO CANADIAN ECONOMY.

7. GIVEN CONSTRAINTS ON CANDEL BY BUDGET SECRECY AND THIS ITS INABILITY TO GIVE SOME DETAILS ON GOC POLICY FOR IMMEDIATE FUTURE, EMBASSY BELIEVES THAT ANSWERS TO FOLLOWING QUESTIONS WOULD PROBABLY BE FORTHCOMING:

(A) WHAT IS PRESENT ESTIMATED CURRENT ACCOUNT DEFICIT FOR 1975 AND ARE NEW CAPITAL FLOWS (E.G. BORROWING IN FOREIGN MARKETS BY PROVINCES) BEGINNING TO COVER? (GOC OFFICIALS HAVE BEEN TALKING ABOUT CURRENT ACCOUNT DEFICIT IN RANGE OF \$4-5 BILLION RATHER THAN \$6 BILLION PROJECTED BY SECRETARIAT.)

(B) WHAT WILL BE EXTENT OF 1975 PROVINCIAL BORROWING ABROAD? (FINMIN TURNER PROMISED LST YEAR TO SET UP "INFORMATION CENTER" TO KEEP FEDERAL AND PROVINCIAL GOVERNMENTS APPRISED OF FOREIGN BORROWING PLANS.)

(C) GOC BXP STATISTICS SHOW THAT IN 1974 THERE WAS MORE CANADIAN DIRECT INVESTMENT ABROAD THAN FOREIGN DIRECT INVESTMENT IN CANADA. WHAT WERE THE REASONS FOR THIS? HASE THE SITUATION WITH RESPECT TO SCREENING OF FOREIGN INVESTMENT IN CANADA HAD ANY DISCERNIBLE EFFECT ON DIRECT INVESTMENT INFLOW? WHAT ARE THE FUTURE PROSPECTS? (PHASE I OF FOREIGN INVESTMENT REVIEW ACT IS IN EFFECT AND REQUIRES REVIEW AND APPROVAL BEFORE A FOREIGN INVESTOR MAY TAKE OVER AN EXISTING ENTERPRISE IN CANADA. PHASE II WHICH COVERS NEW INVESTMENTS OR EXPANSION OF EXISTING FOREIGN-OWNED ENTERPRISES INTO NEW LINES OF ACTIVITY IS NOT YET IN FORCE; THERE ARE REPORTS THAT THE DELAY IS DUE TO DIFFERENCES WITHIN THE CABINET -- ITC MINISTER GILLESPIE FAVORING EARLY IMPLEMENTATION, FINANCE LIMITED OFFICIAL USE

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MINISTER TURNER FAVORING DELAY.)

(D) GOC POLICY HAS MAINTAINED DOMESTIC OIL PRICES AT ARTIFICIALLY LOW LEVELS AND THUS HAS INSULATED CANADAIN ECONOMY TO SOME EXTENT FROM INFLATIONARY IMPACT OF HIGHER WORLD OIL PRICES. THE DOMESTIC PRIVE WILL PROBABLY BE RAISED SIGNIFICANTLY BEFORE THE YEAR IS OUT.WHAT WILL BE THE ECONOMIC IMPAC OF SUCH AN INCREASE?

(E) WHAT EFFECT HAS RECENT RAPID DECLINE IN FOREIGN EXCHANGE VALUE OF CANADIAN DOLLAR HAD ON IMPORTS, EXPORTS, INTEREST RATES, CAPITAL INFLOWS, AND INFLATION?

(F) SINCE HOUSING INDUSTRY IS APPARENTLY MOST DEPRESSED SECTOR OF ECONOMY,WILL GOC TAKE FURTHER STEP TO STIMULATE CONSTRUCTION? HOW DOES CANDEL

RECONCILE CURENT HIGH INTEREST RATE POLICY OF
BANK OF CANADA WITH EFFORTS IMPROVE HOUSING
INDUSTRY?

(G) DOES CANDEL FORESEE INFLOW OF PETRODOLLARS,
REALTIVELY MINOR THUS FAR, INCREASING IN LATTER
PART OF 1975?

(H) WHAT WILL BE GROWTH OF MONEY SUPPLY FOR
1975 AND WHAT WILL BE GENRAL POLICY OF BANK OF
CANADA RE INTEREST RATES FOR THE YEAR?

(I) WHAT WILL BE EXTENT OF GOC BUDGET DEFICIT,
IF ANY, THIS YAR DUE INCOME TAX REBATES AND
OTHER NOVEMBER BUDGET STIMULI?

(J) WHAT EFFECT HAS INCOME TAX INDEXING HAD
ON BUDGET RECEIPTS?

8. ALTHOUGH FINMIN TURNER HAS REFUSED IN PARLIAMENT
TO MAKE PREDICTIONS ON REAL GNP GROWTH,INFLATION AND
UNEMPLOYMENT FOR 1975, CANDEL MAY VENTURE EDUCATED
GUESS ON THESE SUBJECTS.
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